

**EXCERPTS FROM THE TESTIMONY OF  
MR. SAMUEL REA,  
PRESIDENT, PENNSYLVANIA RAILROAD SYSTEM.**

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**BEFORE THE  
Interstate Commerce Commission,  
WASHINGTON, D. C., NOVEMBER 15, 1917.**

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**FINAL CROSS EXAMINATION AND RE-DIRECT EXAMI-  
NATION IN THE FIFTEEN PER CENT. ADVANCE  
RATE CASE (EX PARTE 57).**



Mr. Samuel Rea, President of the Pennsylvania Railroad System, was the first witness to appear for the Railroads on the re-opening of the Fifteen Per Cent. Rate Case, October 17th, 1917.

He was called for final cross examination on November 15th, 1917, before the full Commission. The cross examination was conducted by Mr. Clifford Thorne, representing certain of the shippers, assisted by Mr. J. V. Norman, also of counsel for the shippers. The re-direct examination was conducted by Mr. George Stuart Patterson, General Solicitor of the Pennsylvania Railroad.

Excerpts from Mr. Rea's testimony, bearing upon matters of general interest, are herein reprinted for the information of the public.



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MR. SAMUEL REA,  
President, Pennsylvania Railroad System.

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CROSS EXAMINATION.

The Equipment Situation.

MR. THORNE:—In your former testimony, your attention was called to a large number of purchases of freight cars made a year or so ago, anticipating the requirements, and your attention was called to the fact that purchases during the last year exceeded those of any prior year. In fact, some of the purchases of many of the important commodities exceeded that of several prior years. Now, I will ask you if you will state to the Commission how many cars you think that you would purchase and add to your equipment if this advance was granted, during the coming year?

MR. REA:—I cannot, because it is contingent on a number of things. First of all, there is no use of ordering freight cars today, notwithstanding the extremely high price that they would

cost; unless the Government would give priority on the steel plates, it would be impossible to get them, and even if they did give priority, I cannot figure out that we could get any deliveries before probably the middle of next year, and the price, even at the Government price of steel, would be two and a half the times the price of the last freight cars that we purchased.

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MR. THORNE:—Mr. Rea, in your testimony before, you said that there was doubt amongst railway executives as to the advisability or the practicability of buying more cars and engines at this time, whether they had the money or not, in view of the high cost of equipment and in view of the improved methods that were being put into effect, and other factors. Now, I ask you what is your judgment as to whether you would place orders for additional freight cars if this advance is granted?

MR. REA:—I could not answer that offhand.

MR. THORNE:—I will ask you the same question as to locomotives, Mr. Rea.

MR. REA:—As to locomotives, we have already engaged space for the latter half of next year, the earliest period in which we could expect to get any deliveries, and that contingent entirely upon the foreign locomotives. We placed orders for a hundred. Our own shops at Altoona are turning out an average of twenty-two locomotives every

month for the System. We turned out thirty locomotives in the month of September ourselves, most of which, however, were shifting engines, and the remaining orders are for large freight engines and large passenger engines. We are also building our own steel cars up to our full capacity at those shops, but difficulty in securing labor is making it very difficult to keep up our work and keep up the repairs on our locomotives.

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## RE-DIRECT EXAMINATION.

### Earnings and Property Investment Return.

MR. PATTERSON:—Mr. Rea, I will ask you to turn to this statement, please. I will ask you what is the return on property investment for the year ending June 30th, 1917?

MR. REA:—5.7 per cent.

MR. PATTERSON:—Will you kindly look and see if that is not lower than the return for 1910 or any year prior thereto?

MR. REA:—It is lower than in any year prior to 1911.

MR. PATTERSON:—I will ask you, Mr. Rea, to turn to your printed statement of your testimony given on Monday, November 5th, page 6. Your average dividends paid [for the companies in the Pennsylvania System] during the year ending June 30, 1917, was what?

MR. REA:—6.48 per cent.

MR. PATTERSON:—And that left a surplus of what per cent. of your total capital obligations?

MR. REA:—1.83 per cent.

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MR. PATTERSON:—Has each month shown a decrease in operating income?

MR. REA:—Every month from January to September, inclusive, showed a decrease in net operating income, except the month of July, which showed an increase of \$29,292.

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MR. PATTERSON:—Have you had an estimate made, Mr. Rea, of the situation for October?

MR. REA:—I have. I just got it this morning.

MR. PATTERSON:—And that shows what?

MR. REA:—Total operating revenues, \$44,481,605, an increase of \$5,724,145, or 14.77 per cent. Total operating expense, \$34,070,510, an increase of \$6,844,929, or 25.14 per cent. Net operating income, \$7,504,017, a decrease of \$1,881,399, or 20.05 per cent.

#### **Great Sums Necessary for Improvements.**

MR. PATTERSON:—Mr. Rea, the Pennsylvania System has expended what amount since January 1, 1907, for additions to its property investment account?

MR. REA:—About five hundred million dollars.

MR. PATTERSON:—Since January 1, 1917?

MR. REA:—No; these are June 30th years.

MR. PATTERSON:—I am asking you since January 1st, 1917.



MR. REA:—I beg your pardon. You mean for the current year 1917.

MR. PATTERSON:—Yes, sir.

COMMISSIONER ANDERSON:—You mean for the System?

MR. PATTERSON:—Yes, sir.

MR. REA:—I would like to explain that in this way, that on January 1st, 1917, we had carried over from the previous year appropriations for improvements and betterments for road and equipment, \$74,170,386. Since that date, there has been appropriated \$84,794,562, and there has been expended to September 30th, \$55,117,695, leaving a balance of \$103,847,253 appropriated items for expenditures for additions and betterments chargeable to road and equipment.

MR. PATTERSON:—What has been the average expenditure for road and equipment of the Pennsylvania System for the last seventeen years?

MR. REA:—\$53,000,000.

MR. PATTERSON:—Will you please state to the Commission what expenditures must, in your judgment, be made if the Pennsylvania System is to adequately perform its functions during the ensuing year?

MR. REA:—Well, very much more than \$53,000,000 per year.

MR. PATTERSON:—Of what nature are these expenditures which must be made?

MR. REA:—They are for improved terminals, running tracks, engines, cars, various improvements to the lines, third tracking, fourth tracking, and all other improvements to keep the whole property in balance, and to meet the expanding business, which, as is well known, doubles about every twelve years.

MR. PATTERSON:—Does this proposed rate increase, the question of securing additional net operating income, to the railroads, bear any relation to the question of securing additional facilities, whether of road or equipment?

MR. REA:—Unquestionably. It strengthens the credit of the road and enables it to continue the policy which has given it its position today in the financial world.

MR. PATTERSON:—Is it or is it not going to be absolutely necessary, when the time comes to make all of these improvements out of earnings, to reimburse the treasury by the sale of securities when they are available?

MR. REA:—That seems to be the only means at present, the Government practically, and necessarily, closing the financial market to all other financing.

MR. PATTERSON:—Have these improvements on the Pennsylvania System, or any part of them, got to be made, or do you propose to sit still here for the next year or two years? What will happen if you do?

MR. REA:—We would choke up and have to stop business.

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### War Taxes and the Railroads.

COMMISSIONER ANDERSON:—What part of the war tax do you think the roads should stand, if any?

MR. REA:—I think all of the normal tax. You see, there are various kinds of taxes, the excess profits tax and special taxes.

COMMISSIONER ANDERSON:—You do not mean that the roads should stand those normal taxes out of the increased rates?

MR. REA:—No.

COMMISSIONER ANDERSON:—You mean that those should be included in operating expenses?

MR. REA:—Yes, sir. Of course, they will be included ultimately in operating expenses, but it is presumed that this is a temporary tax, and the railroads should bear the burden as all other institutions do, due to the war.

COMMISSIONER ANDERSON:—You would not say, then, that it would be just to pass on to the rate payer the excess profit tax or the special war tax?

MR. REA:—No, I would not think so.

MR. PATTERSON:—Who has to pay it, Mr. Rea, if the public does not pay it?

MR. REA:—Well, the railroad companies, I think, will have to stand their share while the war is on.

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## RE-CROSS EXAMINATION.

### Discussion of Railroad Financing.

MR. THORNE:—During these last few months have you borrowed any money—in the last three or four months?

MR. REA:—No; we did not need to. We still have \$26,000,000, the proceeds of our bonds sold last spring, which is earmarked for such expenditures for road and equipment as are prescribed by the mortgage.

MR. THORNE:—And as I understand it, if this advance is granted, it would not enable you to market, or you would not try at the present stage of the market, to issue a new bonded indebtedness?

MR. REA:—No; we do not need it. Just as soon as we do need more money, we will be in the market—probably next spring.

MR. THORNE:—Yes; but at the present time is it your judgment that the railroads, or any other class of industrials or public utilities, would be able to sell securities at a reasonable rate, whether this advance is granted or not granted?

MR. REA:—I would answer that more positively by saying that they should not go into the markets while the Government is trying to secure money to prosecute the war.

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## Government Loan to Railroads.

MR. THORNE:—Now, I want to know, if the Government, feeling that the purchase of equipment should not be made out of earnings, and that there is not a sale for private securities of either public utilities, industrials or railroads—if the Government should lend you the money, would you object?

MR. REA:—It would depend entirely on the terms. My own opinion is that, if the Government,—and I am speaking personally and as one executive only—if the United States Government, feeling that there is an absolute necessity for more freight cars, for instance, would loan to the railroad companies money at not exceeding the rate the Government itself is paying for money, and in large sums, on what we would call the car trust principle, whereby the railroads and the Government would, in addition, secure the Government price for the commodities that go into those cars, and would then allocate the cars to the railroads of the country on what is known generally as the car trust plan—but still more liberal than any car trust plan ever yet evolved—namely, that on a ten-year period the annual increments of the principal should be paid by the railroad companies, and that a pro rata number of cars should be released so as to enable those railroad companies to raise their capital, then I think the railroads of the country ought to agree to accept

the money on that plan, and there should probably be 100,000 new freight cars built. Otherwise, I cannot see how it is possible to get any increase in the freight equipment of the country.

COMMISSIONER McCHORD:—If the Government would do just as you stated, would that meet your requirements or the necessities of the railroads?

MR. REA:—I doubt it, Mr. Commissioner. I doubt whether it would be sufficient. It would not, unless the railroads could correspondingly bring up their terminals, yards and other facilities. Then comes in the element of time. As I said a moment ago, you cannot get to those cars, perhaps, until the second half of next year. You cannot get any locomotives for American railroads until the second half of next year.

COMMISSIONER McCHORD:—You could get it quicker with Government money?

MR. REA:—Yes, sir; because I assume that, going with the Government money, would come the priority of the steel, and of course priority of transportation as well. I assume 100,000, Mr. McChord is empirical, it is arbitrary. Fifty thousand might ease the situation very much. You will find some transportation men who will say that if 100,000 cars were pitchforked into the situation as it is today, it would make it worse.

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MR. THORNE:—In that proposition or outline that you gave, there is just one qualification I wanted to make, and that is if it would not be



fair, instead of adopting the [interest] rate that the Government paid, to adopt the rate which, say, a given railroad paid prior to our entrance into the war?

MR. REA:—Why, no, I do not think so at all. I am assuming that the Government would treat its railroad systems in its own country as liberally as it is treating its Allies in this war, and this would be a war measure.

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COMMISSIONER ANDERSON:—Mr. Rea, you sketched the possible basis of a government loan to the companies. I was not quite sure whether you intended to say that in your judgment the time has come and conditions are ripe so that it is necessary or desirable, either or both, that such relief by the Government to the companies should be extended. I would like to get your view on that.

MR. REA:—It is my individual judgment as a railroad executive that the time has certainly come for consideration of that matter, and it would have to be, as I have outlined, on a very liberal basis.

COMMISSIONER ANDERSON:—Is one of your reasons for so thinking the fact that the Government has been using up your equipment for various war purposes and has also limited the opportunity to get additional equipment by extending help to the Allies?

MR. REA:—Yes, sir; that is brought about by the war, Mr. Commissioner, unquestionably. There is a larger demand for transportation than we can supply.

COMMISSIONER ANDERSON:—Assuming, then, that your view should be the view of the next Congress, and that help of that kind should be extended, even if it did not meet all the bases of your desire to increase the rates, it would substantially modify the rights of the railroads to an increase of rates, would it not?

MR. REA:—No; I had not thought it would modify them in the slightest degree.

COMMISSIONER ANDERSON:—Why not?

MR. REA:—Because I think the railroads need the increase anyhow. You see, you are dealing with an exceptional railroad. You must agree to that. The weaker roads are drifting into a dreadful state in this country, and as to the people who are tributary to those weaker lines, the transportation is just as necessary to them as it is to the ones on the stronger railroads.

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### **Equipment and Labor Shortage.**

COMMISSIONER ANDERSON:—You spoke of the government's furnishing capital for supplying the needed additional car equipment. Is it your view that there are cars available now in the country by all the railroads, still not utilized; in other words, if you could operate the car system of



the country as in effect, would it substantially diminish what would otherwise be the needs of additional equipment?

MR. REA:—Well, I am beginning to doubt it. My seven months' experience here in this work leads me to believe that there must be more cars. We are wearing them out, unquestionably, rapidly. We have not the help to properly repair them. And as I stated in my direct testimony, I think, with reference to engines, they are sent out on the roads without really proper preparation; and the same applies to cars. We are not renewing them rapidly enough, and there has been a terrible drain on our shops and on our railroad facilities which we have not been able to meet.

The same way with the deferred maintenance of the railroads. We are working women on the tracks—115 women working on the tracks between Pittsburgh and New York. We are trying to work them in the lighter kind of track work. Of course, they cannot handle rails, and probably have not been able to tamp ties yet, but they are learning, and we are taking every measure possible, and there is not a day when we are not called upon by the government to help by giving them additional men; and they even inquired lately as to whether we could not turn our shops on munitions. We would like to help in every direction, but we cannot let the transportation system break down.

COMMISSIONER ANDERSON:—Undoubtedly there

has got to be additional equipment, because this is wearing out very rapidly. Illustrate it by this: Suppose the Government bought all the cars of the country and operated them in the same general line that you propose to operate those which might be furnished on the Government credit, would you get a substantially increased use of cars over that which you are now getting?

MR. REA:—Very little, I think.

COMMISSIONER ANDERSON:—In other words, you think the rolling stock of the country is now being utilized to its best advantage?

MR. REA:—I think so, although we are all hopeful of getting a better mileage out of the cars. Of course, we are getting a better loading. The shippers are helping splendidly in that.